The 4th Anti Laundering Directive, more of the same?

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The 4th EU Laundering Directive has now been passed and will come into effect on 26th June 2017. We still await the publication of the new UK Money Laundering Regulations which will put the Directive into effect in this country but the basis of the new law is clear and the UK's forthcoming departure from the EU is unlikely to make any difference as this is an area where there is no significant distinction between the member states' views on the topic. The contents of the Directive represent a minimum that must be adopted although Member States are permitted to go further should they wish.

The first key development consists of a requirement that due diligence arrangements be enhanced which must now be done before work is carried out for a client, although there is a caveat permitting work to start for a client pending proof of identity where this is necessary. There is also an exception when a client is utilising the skills of independent legal professionals in judicial proceedings. Auditors, external accountants and tax advisors only need to carry out due diligence to the extent of determining who their client is.

It is also necessary for a regulated firm to determine what the purpose and intended nature of the business relationship is. This includes conducting ongoing monitoring of that relationship, including scrutiny of transactions undertaken throughout its course to ensure that the transactions being conducted are consistent with the obliged entity's knowledge of the customer, the business and risk profile, including where necessary the source of funds and ensuring that the documents, data or information held are kept up-to-date. Regulated firms are also required to understand the background and purpose of all complex and unusually large transactions.

There is also an increased emphasis being placed on determining the beneficial owners of funds, which is something of a problem as those who are moving money for illegal purposes will not declare themselves as such. Nor is there usually any way of determining whether the person dishonestly acting as an agent is not really the principal.

This reported information must be held in a central register which in this country will be at the National Crime Agency. States can arrange an exemption to the access of all or part of the information on beneficial ownership on a case-by-case basis in exceptional circumstances, which are essentially those where it would put the owner of the money at risk eg, of fraud, kidnapping, blackmail, violence or intimidation, or where the beneficial owner is a minor or otherwise incapable.

Perhaps most alarming is the extension of the requirements relating to politically exposed persons ("PEPs") to cover domestic individuals including those who departed from such a position in the previous twelve months. This is going to cause problems as the wide range of people caught and the 'hair trigger' reporting requirement in relation to this category, coupled with the extremely wide common law definition of "suspicion" guarantees that a significant number of law abiding UK people will find themselves being reported and their bank accounts being frozen. On the other hand, even with modern internet based checking systems many individuals who come within the definition of a PEP will slip though the net, especially those caught by the wording of "persons known to be close associates" of one of the main named parties on the PEPS list. For a regulated firm there may be some safety in the word "known" but even so the ambition expressed by this part of the Directive seems to be unrealistic.

Any business selling goods for cash will have to make a suspicious transaction report whenever a sale is made which exceeds €10,000. Virtual currencies are now brought within the anti money laundering system, though this is unlikely to affect many businesses. All gambling is covered by the system from the commencement of the new Directive, not just casinos as at present.

The various Financial Intelligence Units in the EU, which in this case will mean the National Crime Agency are to be given more power and access to greater information. This appears to include a centralised system to cover all the accounts held by one person representing a further erosion of civil liberties as previously such information would only be held by HM Revenue and Customs.

Regulated firms must take reasonable measures to determine whether the beneficiaries of a life or other investment-related insurance policy and, where required, the beneficial owner

of the beneficiary are politically exposed persons. It seems somewhat unrealistic to regard life policies as a suitable vehicle for money laundering. Such arrangements do not pay out until the death of the party creating the policy or on the death of the relevant person where it is taken out by someone financially dependant on them. The limited extent to which they have an investment value is that it is possible with many policies to cash them in or sell them for a fairly high proportion of their payout value if there is proof that the person concerned has less than six months to live.

It is possible to be concerned about the imperative behind the new Directive. The Financial Action Task Force (" FATF"), was originally intended as a temporary body to establish a set of recommendations on which to develop anti-laundering laws. After repeatedly having its original four year term extended it now operates as a body whose main function seems to be to provide jobs for its employees by finding the need for repeated extensions to the existing laws. As long as the FATF exists there will be repeated demands for developmemts to the existing law.

We therefore now have another set of laws designed to combat or at least reduce the incidence of money laundering and terrorist financing. There is just one problem; the existing law seems to be having little discernible effect. That in itself is not a conclusive reason for not having them; it is possible to justify the laws on the basis that matters might be even worse if they did not exist. However, these laws represent a considerable intrusion into personal liberty. The entire population who have bank or building society accounts, use financial services or a very wide range of facilities involving money find themselves being spied on and their details kept on a central database. To make matters worse the basis of this spying is an absurdly wide common law definition of "suspicion" which seems to little more than the mildest sense that something may be untoward. Suspicious transaction reports are then submitted to a government agency on an enormous scale to very little evident benefit. There seems to be no convincing evidence that this is resulting in a significant attack on drug gangs organised crime or terrorism. Countries which have gone further and imposed a bulk cash transaction reporting requirement such as the USA and Australia seem to have fared no better.

The recent National Crime Agency annual report shows that over a third of a million suspicious transaction reports were submitted, of which over 82% were submitted by banks.

An analysis of the annual report shows that of those reports where request to continue acting was granted to the reporting firm, just over £100,000 was seized and just over £1 million repatriated to HMRC. Nor is there any evidence provided in the annual report as to how many arrests in previous years have since led to a conviction. The strongest arguments for utilising suspicious transaction reports are those cases where victims of crime have monies reimbursed from criminals due to suspicions having been reported by third parties. What is less clear is how many of these would have been dealt with by other methods, eg, normal police procedure or the victim seeking legal redress. Certainly, there seems no evidence to support the industrial scale domestic spying which is now taking place.

The simplest solution might be to adopt a much more restrictive definition of "suspicion" for the purpose of transaction reports and so limit the internal spying and reporting that is taking place. Providing a statutory definition to replace the current common law one would assist in this. At the moment the NCA seem to regard the volume of such reports as evidence of the virility of the system when what is really needed is less material but of a higher quality.

In part this Directive is a logical development of its predecessor, the 3rd Directive, and the publication of the Panama papers gave added impetus to the idea that the laundering laws needed to be further developed when it became apparent that there was insufficient understanding of the complex, hidden structures that were used by people to hide money. Another element in the thinking behind the Directive has been the view of the FATF that further developments are needed in this area. Indeed, the contents of the Directive largely follow the FATF recommendations. The problem is that the new Directive has no likelihood of achieving this.